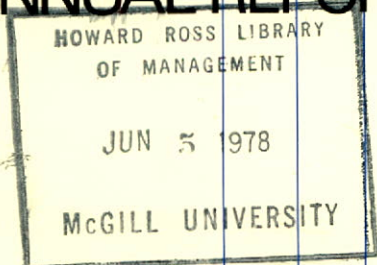


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# 1978 ANNUAL REPORT



# INTERCO 67th Annual Report

**The Annual Meeting of Stockholders**

will be held at 10 a.m., Monday, June 19, 1978 at the Breckenridge Pavilion Hotel, One Broadway, St. Louis, Missouri. Notice of the meeting and a proxy statement will be sent to stockholders in a separate mailing.

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# Highlights

## Fiscal Years Ended February 28

	1978	1977	Change
From operations:			
Net sales . . . . .	<b>\$1,666,657,000</b>	\$1,566,432,000	+ 6.4%
Earnings before income taxes . . . . .	<b>161,579,000</b>	149,392,000	+ 8.2%
Net earnings . . . . .	<b>81,834,000</b>	76,270,000	+ 7.3%
Percent of net sales . . . . .	<b>4.9%</b>	4.9%	
Per share of common stock:			
Fully diluted earnings . . . . .	<b>\$5.70</b>	\$5.32	+ 7.1%
Dividends . . . . .	<b>\$1.85</b>	\$1.62 1/2	+ 13.8%
Financial condition at year end:			
Working capital . . . . .	<b>\$ 532,361,000</b>	\$ 481,156,000	+ 10.6%
Current ratio . . . . .	<b>4.2 to 1</b>	4.4 to 1	
Total assets . . . . .	<b>899,778,000</b>	819,360,000	+ 9.8%
Stockholders' equity . . . . .	<b>621,512,000</b>	565,178,000	+ 10.0%
Book value per common share . . . . .	<b>\$43.34</b>	\$39.72	+ 9.1%
Return on stockholders' average investment . . . . .	<b>13.8%</b>	14.2%	
Shares outstanding at year end:			
Common stock . . . . .	<b>14,341,155</b>	13,886,459	
Preferred stock . . . . .	<b>—</b>	136,131	



# To Our Stockholders

Fiscal year 1978 was another year of achievement for INTERCO as new records were again established in earnings and sales and earnings per share—for the fourteenth consecutive year. These new performance levels were reached by constant attention to our budgeted plans in a very difficult, challenging climate of cost escalation.

INTERCO's record results were somewhat less than planned due to weather-related problems in the fourth quarter. Our record performance in the fourth quarter was adversely affected in manufacturing, distribution and retailing by the severe winter weather conditions during the months of January and February—the last two months of our fiscal year.

Sales for the fiscal year were \$1.67 billion, net earnings were \$81.8 million and earnings per common share were \$5.70. Fiscal 1978 was another important year for the company in achieving its planned growth target of attaining consistent annual improvement in earnings per share. The new records in earnings and sales are a reflection and tribute to the dedicated management in each of our businesses.

As we have reported many times, our management places great importance on people and their motivation, together with constant communications within the entire organization. The function of the monthly Operating Board, which budgets, reviews, plans and shares ideas, continues to be an integral part of management's operating philosophy. In addition, the small corporate staff coordinates corporate objectives, with the complete involvement and cooperation of the operating managements.

The financial strength of your company grew even stronger during fiscal 1978 achieving growing liquidity, a satisfactory working capital ratio and excellent debt-equity leverage. We will be able to finance growth from internally generated funds for the foreseeable future. Cash and short-term investments totalled almost \$114

million at year end, and the company had no domestic short-term borrowings during the year.

Cash dividends on the company's common stock were increased 20.5% during fiscal 1978, and the current annual rate is \$2.00 per share. INTERCO has paid cash dividends on its common stock for sixty-seven years without interruption and has increased cash dividends for the past thirteen consecutive years—from \$0.60 to \$2.00 per share or an increase of 233%. Your Board of Directors will continue to make frequent reviews of the dividend rate, in conjunction with the expected continuing growth of the company.

We are pleased to report that another long-established apparel manufacturer—International Hat Company—joined INTERCO on March 31, 1978, after the close of the fiscal year. This company is a manufacturer and distributor of a complete assortment of men's and women's sport and casual headwear. This expands INTERCO into a new market, with new profit and growth opportunities.

INTERCO's business is manufacturing and retailing popular-priced products and services which are basic, everyday necessities for the middle-income consumer; and our businesses do not necessarily depend on a booming economy to grow or to maintain their position of leadership.

Continued growth is planned for fiscal 1979. We have the financial resources, the in-depth management capability, and the products and services to do an improving job. As in the past, INTERCO will be managed in a decentralized fashion, with the operating companies fully responsible for day-to-day operations. Our plans for next year include:

- ☐ Intensifying our rigid cost control and cost reduction programs.
- ☐ Continuing to assure sound employment of our assets and redeployment of assets which have not given us a satisfactory return.



- ☐ Continuing to seek out and evaluate acquisition possibilities which will add strength and establish new markets or provide a strong new base of operations for the company.
- ☐ Putting cash to work in improving efficiency with the newest manufacturing and distributing equipment, new and relocated retail stores, refurbished retail locations, new products and services and constant marketing reviews.
- ☐ Maintaining inventory levels in line with projected sales expectations and to track constantly, our inventory turnover.
- ☐ Increasing our awareness of markets, competition and customer needs.

Our prime objective is to operate a well-balanced diversified company, with increasingly, higher earnings and improved return on stockholders' investment, through profit-oriented managements and cost containment.

We are budgeting our business for continuing growth and we expect fiscal 1979 to be another good year for INTERCO.

I wish to thank our loyal and conscientious employees for their efforts during the past year. We wish to thank also our customers for making it all possible, and our shareholders for their continuing support and confidence.



WILLIAM L. EDWARDS, JR.

*W. L. Edwards, Jr.*

Chairman of the Board and  
Chief Executive Officer

April 12, 1978



# INTERCO Today

INTERCO is a broadly based major manufacturer and retailer of popular-priced products and services for the middle-income consumer, represented by three operating groups:

## Apparel Manufacturing Group

consists of eleven apparel companies operating 62 manufacturing plants and 13 major customer distribution centers across the country. The group designs, manufactures and distributes a full range of branded and private-label sportswear, casual apparel, outer garments and headwear for men and women. Distribution is national in scope to department stores, specialty shops and other retail units. Substantial distribution, under private label, is also made to large national retail and discount chains.

## General Retail Merchandising Group

operates 732 retail locations in 29 states in this country, offering to the consumer a large assortment of popular-priced products and services. General retailing includes junior department stores, discount stores, men's specialty apparel shops, specialty department stores and large do-it-yourself home-improvement centers. Ten modern regional distribution centers support these retail locations in several regions in the country.

## Footwear Manufacturing and Retailing Group

operates 865 retail shoe stores and leased shoe departments in 40 states in this country, as well as in Australia, Canada and Mexico. The group also styles, manufactures and distributes, primarily, men's footwear in most major price ranges in the United States, Canada and Australia. The group also produces footwear for women and children. There are 30 shoe manufacturing plants and 6 major distribution centers in operation.

## General

INTERCO employs 44,000 men and women, and there are approximately 16,500 stockholders.

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## Major Brands

**London Fog®**



**CAMPUS®**

**BIG YANK®**

**BILTWELL®**

**Tailor's Bench®**

**it's  
pure  
Gould®**

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## Major Store Names

**Thornton's**



**VALUE CENTER**

**P.N. HIRSCH & CO.**  
*Department Stores*



**Golde's**

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## Major Store Names

**FLORSHEIM SHOES®**

**FLORSHEIM THAYER McNEIL**

**THOMPSON BOLAND LEE**





QUEEN CASUALS®

college town™

Mr. Tennis®

ROUGH RIDER®

John Alexander®

Stuffed  
Shirt®

STUFFED  
JEANS®

LADY QUEEN®

panther™

Mr. Golf®

Clippers Mist®

DEVON®

lady  
devon®

Startown™

Leonard Macy™

STUFF  
SPORTSWEAR®

SKY CITY DISCOUNT  
CENTER

Fine's men's  
SHOP

Carithers

Keith O'Brien

United Shirt

JEANS GALORE

WIGWAM  
STORES

KENT'S

EAGLE FAMILY  
DISCOUNT  
STORES

CENTRAL HARDWARE

Miller's

Standard Sportswear

Shainberg's

#### Major Brands

The Royal  
Imperial  
FLORSHEIM SHOE®

FLORSHEIM® IDOLERS  
BY FLORSHEIM®

Julius Marlow®

CRAWDADS®

CITY CLUB®

RAND®

WORTHMORE™

Grizzlies™

RED  
GOOSE®

ROBERTS™

Miss  
Wonderful™

savage®

Personality™

WINTHROP®

Ambassador®

PATRIOT®

Poll-Parrot®

McHale™

DIVINA®

HY-TEST® VITALITY®



# Apparel Manufacturing Group

Sales Volume: \$640,487,000  
Operating Profit: 86,745,000

INTERCO's Apparel Manufacturing Group is a major producer and distributor of men's and women's sports and casual wear; and outerwear to department stores, specialty stores and other large retail chains across the country.

Fiscal 1978 was another record performance for both the men's and women's apparel portions of our business — setting new records in sales and earnings.

The group contributed \$640.5 million or 38.4% of the consolidated sales and \$86.7 million or 51.2% of the earnings of the company, a return on sales before income taxes, corporate expenses and interest cost of 13.5%. The sales increase amounted to 11.2% and the earnings gain was 11.1%.

INTERCO's apparel companies continue, each year, to increase their share of the moderately-priced apparel market by offering value, quality, and modern fashion — relaxed clothing is the key to fashion. An ever-widening circle of exciting leisure activities characterizes today's life style, demanding diversity of apparel fashions. Casual apparel and sportswear has been and will continue to be the principal market served by the apparel companies of INTERCO.

Our apparel productivity continues to improve through the acquisition of the newest and latest cutting, sewing, knitting and finishing equipment available. Centralized computer-operated pattern grading and marking systems, as well as installation of automatic and semi-automatic equipment for other manufacturing operations have been introduced to help control and reduce cost. Current plans include two additional apparel manufacturing plants during fiscal 1979 to satisfy increasing demand.

Distribution facilities are the most modern and efficient in the industry today, and will be expanded as needed. One such new

large, automated distribution center was opened in Randolph, Massachusetts during fiscal 1978, to service customers of *Pant-Her*, the nationally-advertised sophisticated young missy line from *College-Town*.

Currently emerging apparel style trends for both men and women have been met by INTERCO. Both trends — for men and women — can be characterized as a dress-up fashion trend. Feminine apparel is moving to a more classic look with a heightened emphasis on skirts and dresses. Male apparel is moving to a gentleman's look which, at the same time, is a casual, easy, comfortable dress-up look. Neither gender, however, is abandoning jeans, active sportswear, or casual collections of coordinates.

INTERCO's women's apparel serves three markets — the young junior, the junior and the more sophisticated missy market — and offers suits, dresses, pants, skirts, jackets, sweaters, hats — sport, sun and rain — blouses, shirts, T-shirts, jumpers, vests, jeans, culottes, blazers, rainwear, golf jackets and light and heavy outerwear.

The company's men's apparel offers everything from a classic casual dress-up look to the rugged image, and includes shirts — sport, knit, and dress — slacks, sweaters, sport coats, blazers, three-piece vested casual sport suits, jeans, western wear, golf jackets, hats — western, dress, sport and rain — rainwear, light and heavy outerwear, walk shorts and swim wear.

INTERCO will continue to sharpen its marketing strategy through its manufacturing and merchandising expertise and will continue to capture an increasing share of this vast apparel market for moderately-priced clothing for the discriminating value-conscious and style-conscious American consumer.

We expect another strong performance in fiscal 1979 from our Apparel Manufacturing Group as we offer a complete wardrobe for men and women — everything from "head to toe."





London Fog®





panther

John Alexander.

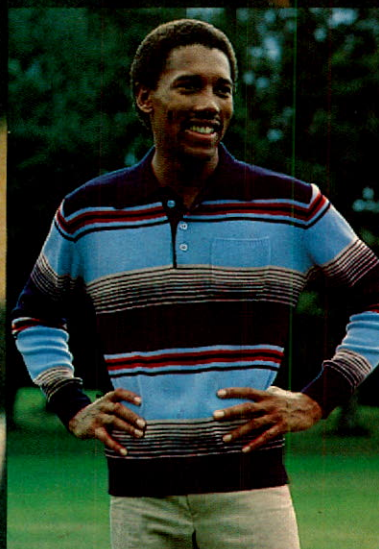
QUEEN CASUALS.



it's  
pure  
could



lady  
deron.



CAMPUS



college town





devon.



Stuffed  
Shirt. STUFFED  
JEANS



# General Retail Merchandising Group

Sales Volume: \$521,178,000  
Operating Profit: 38,096,000

The company's diverse General Retail Merchandising Group posted a record year in fiscal 1978 in both sales and earnings — despite adverse winter-related problems in January and February, the final two months of our fiscal year.

The diversity of operations includes: 388 junior department stores...239 self-service, convenience discount stores...75 men's specialty apparel shops...22 large do-it-yourself home improvement centers...and 8 specialty department stores.

The group contributed \$521.2 million or 31.3% of the consolidated sales and \$38.1 million or 22.5% of the earnings of INTERCO, a return on sales before income taxes, corporate expenses and interest cost of 7.3%. The sales increase amounted to 4.5% and the earnings gain was 17.3%.

INTERCO's general retail operations are regional which affords each management group more flexibility and the ability to react more quickly to consumer needs and market changes. Future expansion potential exists in each of these regional markets for each of our five diverse types of operations.

Providing basic, essential everyday needs to the consumer — our continuing goal — increased our competitive position during the past year. The group will continue to emphasize its program of offering products and services in its retail stores which stress quality at lower prices to meet the shopping needs of the inflation-conscious consumer.

The General Retail Group opened 50 new locations, closed and relocated some marginal retail units and expanded their square footage for centralized distribution by 11% during fiscal 1978. The group expects to open a minimum of 55 new locations during fiscal 1979.

□ *P.N. Hirsch & Company* — a large chain of junior department stores — had a very good year in fiscal 1978, offering its merchandising expertise in basic clothing and household needs to its market — small and medium-sized communities. *P.N. Hirsch* will streamline its distribution operations in the new year by expanding their facility at Vandalia, Illinois.

□ *Central Hardware* had another record year in sales and earnings, and during fiscal 1978 entered another new consumer market — Cincinnati, Ohio — with its large, complete do-it-yourself home improvement centers. Looking

into the future, *Central Hardware* is well positioned for continuing growth as it brings everything needed to maintain, improve and expand the requirements of the do-it-yourselfer. *Central Hardware's* metropolitan markets are now Cincinnati, Indianapolis, Memphis and St. Louis, with more penetration to come in the future in other market areas.

□ *Eagle Family Discount Stores* again posted record sales and earnings in fiscal 1978, and expanded its base of operations with 21 new locations. Ending the year with 191 locations, *Eagle* will bring its everyday, low-priced consumer necessities to a larger market in fiscal 1979, with a minimum of 20 new locations.

□ *Sky City Stores, Inc.*, the multi-state southeastern discount retailer, completed its first full year of operation for INTERCO with the highest sales and earnings in its history. *Sky City* added seven new large discount centers during the past year and its current growth plans include at least six additional large centers during fiscal 1979. *Sky City* will increase their profit margins by improved control of centrally shipped merchandise to their stores, with the completion in May, 1978, of a new large distribution center at Greenville, South Carolina.

□ Our chain of 75 men's specialty apparel shops — *Fine's, Standard, and United* — turned in a record performance in sales and earnings in the past year. These shops provide a complete male fashion line of active sportswear, tailored apparel, and all male accessories in seven states in the East, Mid Atlantic and Central regions of the country.

□ *Golde's* — INTERCO's specialty department store chain — added its eighth store during the year. Despite a fire which totally destroyed its largest store in suburban St. Louis, making it inoperative for six months, *Golde's* had a very satisfactory year. They continue to seek new location possibilities.

INTERCO believes the growth and expansion potential of the General Retail Merchandising Group is concentrating on merchandising techniques and cost control, which will permit the company to continue to bring excellent value and service to its customers, shopping in a pleasant environment, while offering quality at popular prices.















# Footwear Manufacturing and Retailing Group

Sales Volume: \$504,992,000  
Operating Profit: 44,552,000

INTERCO's footwear retailing operations, which number 865 units across this country and in Canada, Mexico and Australia, had another outstanding year—a new record in sales and earnings.

In the production of quality footwear, the company maintained its position during the year as one of the principal shoe manufacturers in this country, although continuing pressure from footwear manufactured abroad had an impact.

The Footwear Group contributed \$505.0 million or 30.3% of the consolidated sales and \$44.6 million or 26.3% of the earnings of the company. This was a return on sales of 8.8% before income taxes, corporate expenses and interest cost. The sales increase was 2.7% and the earnings reduction was 8.6% from a strong performance of one year ago.

Continuing our program of close scrutiny of return on assets employed, some redeployment of footwear manufacturing assets was necessary during fiscal 1978. *Florsheim* announced the discontinuance of its women's shoe manufacturing operation after the Spring 1978 line. The quality women's shoe market has been diminished by foreign-made footwear, resulting in severe manufacturing cost pressures. Also, to improve productivity in our thirty shoe manufacturing plants, three older, multi-story plants were closed during the year. All non-recurring costs from these actions are included in the fiscal 1978 results.

## Footwear Retailing

Our strong retail footwear growth is attributed to significant increases in volume in existing locations, additions of new *Florsheim* and *Florsheim Thayer McNeil* locations in the United States and the opening of prestige *Florsheim Shoe Stores* for men in Mexico City and Australia. Of particular success are the new *Florsheim* and/or *Florsheim Thayer McNeil* units in major downtown malls such as Water Tower Place, Chicago; Gallery, Philadelphia; and Omni in Miami. Shown on page seventeen is one of many luxurious stores of independent shoe retailers—this one is Sherman's in Detroit—which participates in the highly beneficial *Florsheim Dealer Development Program*. This dealer program assists shoe retailers in major store remodeling, and new store design and

construction, and provides operational assistance in achieving maximum profitability.

Senack Shoes, Inc., the company's principal operator of leased shoe departments, had its best year ever in both sales and earnings in fiscal 1978. *Senack* is adding substantially larger volume departments which offer greater potential and is eliminating smaller units.

## Footwear Manufacturing

INTERCO continues to strive to satisfy consumers' demand for quality footwear—dress and work shoes, casual footwear, and boots—primarily for men. The company also produces footwear for women and children.

- Styling, fashion and outstanding value, long recognized as the hallmark of *Florsheim* quality leather footwear for men—as shown to the right—continues as the ultimate responsibility in manufacturing men's footwear. The *Idlers by Florsheim* collection of men's quality casual footwear continues to receive wide dealer and consumer acceptance.
- International Shoe Company* and its family of branded footwear for men, women and children performed on plan in fiscal 1978. Substantial effort continued to be directed to new machinery and manufacturing techniques to lower costs and improve productivity. *Hy-Test Safety Shoes* continue to increase their wide acceptance in a dual role, giving the customer a choice, with safety—for both leisure and work.
- Interco Savage Limited*, our Canadian footwear subsidiary, had a fair performance in sales and earnings in fiscal 1978, despite intensifying, foreign competition in Canada. *Interco Savage's* performance was below the average of the footwear group.

## General

Keenly aware of the volatile domestic shoe manufacturing scene, INTERCO will remain tuned to maximizing its return on investment in this part of its business. We have premium brand names and quality footwear which are important to the consumer who recognizes and knows value and durability.

Our footwear retailing operations are expected to continue to accelerate their record performance during fiscal 1979.



The Royal Imperial  
FLORSHEIM SHOE





**PATRIOT**

Personality

**RAND**

**HY-TEST**  
Safety Shoes

**IDLERS**  
BY FLORSHEIM®



FLORSHEIM.





## Another INTERCO Company International Hat Company

*International Hat Company* joined the Apparel Manufacturing Group of the company on March 31, 1978.

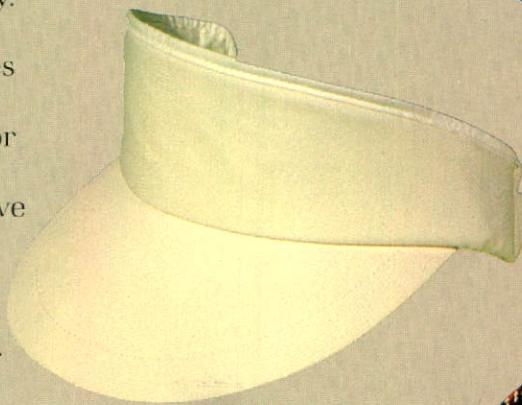
This company, which was founded in 1917, manufactures and distributes a wide assortment of headwear, under private label, for men and women.

An extensive product line, a few of which are shown here, consists of western straws, sun and fun straws, caps of all varieties, cloth hats, tennis hats, visors, town and country casual headwear, knitted headwear and waterproof rain hats.

*International Hat* is considered one of the larger producers of casual and sports headwear in the country. Its sales offices are located in New York City and the company operates six manufacturing plants — five in Missouri and one in Texas. Its major warehousing facility is located in St. Louis, with three small supportive distribution centers elsewhere.

*International Hat* has enjoyed steady growth over the years and is geared to its future with INTERCO.

This acquisition expands INTERCO's ability to provide popular-priced apparel with a new market opportunity — sports and casual headwear for men and women.





# Fiscal 1978 in Review

During fiscal 1978 and for the fourteenth consecutive year, INTERCO achieved record sales and earnings, and at February 28, 1978, was in the strongest financial position in its history.

Net sales were \$1.67 billion, net earnings were \$81.8 million and fully diluted earnings per share were \$5.70.

The comparative financial statements and references to fiscal 1977, shown in this review, have been restated for the effect of capitalization

of leases as required by Statement of Financial Accounting Standards No. 13. The business segment reporting was also restated pursuant to Statement of Financial Accounting Standards No. 14.

The following presents our three operating groups' sales and earnings for a five-year period. These figures have been restated to include pooled companies for years prior to their acquisition and for the retroactive restatement of capital leases.

	Fiscal Years Ended				
	1978	1977	1976	1975	1974
Net sales:					
Apparel .....	\$ 640,487	\$ 576,019	\$ 484,152	\$ 469,171	\$ 427,764
General Retail .....	521,178	498,557	474,230	425,688	399,507
Footwear .....	504,992	491,856	465,870	478,364	477,603
Total .....	<u>\$1,666,657</u>	<u>\$1,566,432</u>	<u>\$1,424,252</u>	<u>\$1,373,223</u>	<u>\$1,304,874</u>
Earnings before income taxes:					
Apparel .....	\$ 86,745	\$ 78,050	\$ 63,715	\$ 53,482	\$ 49,012
General Retail .....	38,096	32,473	35,219	28,534	27,972
Footwear .....	44,552	48,768	43,884	50,545	45,183
	<u>169,393</u>	<u>159,291</u>	<u>142,818</u>	<u>132,561</u>	<u>122,167</u>
Less corporate expenses and interest cost	( 7,814)	( 9,899)	( 7,033)	( 11,474)	( 11,568)
Total .....	<u>161,579</u>	<u>149,392</u>	<u>135,785</u>	<u>121,087</u>	<u>110,599</u>
Income taxes .....	<u>79,745</u>	<u>73,122</u>	<u>67,212</u>	<u>59,853</u>	<u>53,799</u>
Net earnings .....	<u>\$ 81,834</u>	<u>\$ 76,270</u>	<u>\$ 68,573</u>	<u>\$ 61,234</u>	<u>\$ 56,800</u>
As a percent of sales .....	<u>4.9%</u>	<u>4.9%</u>	<u>4.8%</u>	<u>4.5%</u>	<u>4.4%</u>

## Growth Rate

Our average compounded annual growth rate, as reported over the past five years, was 10.7% for sales and 15.9% for net earnings. In addition to the growth performance, the profitability of the company — net earnings to net sales — has improved to 4.9% from 3.9% five years ago.

## Sales

Net sales for the fiscal year were a record \$1.67 billion, an increase of \$100.0 million or 6.4% over \$1.57 billion for the prior year.

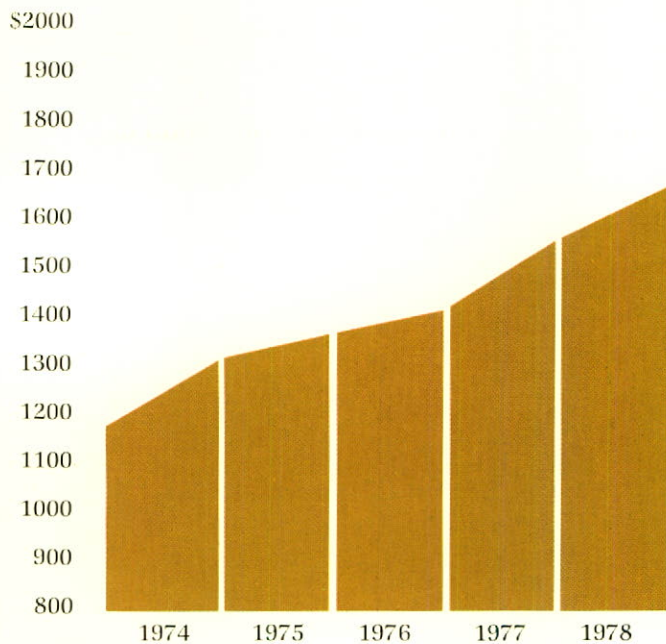
The operating groups of the company contributed sales in millions of dollars, compared with the prior year, as follows:

	Fiscal 1978		Fiscal 1977		% Change
	Sales	%	Sales	%	
Apparel	\$ 640.5	38.4	\$ 576.0	36.8	+11.2
General Retail	521.2	31.3	498.5	31.8	+ 4.5
Footwear	505.0	30.3	491.9	31.4	+ 2.7
	<u>\$1,666.7</u>	<u>100.0</u>	<u>\$1,566.4</u>	<u>100.0</u>	<u>+ 6.4</u>

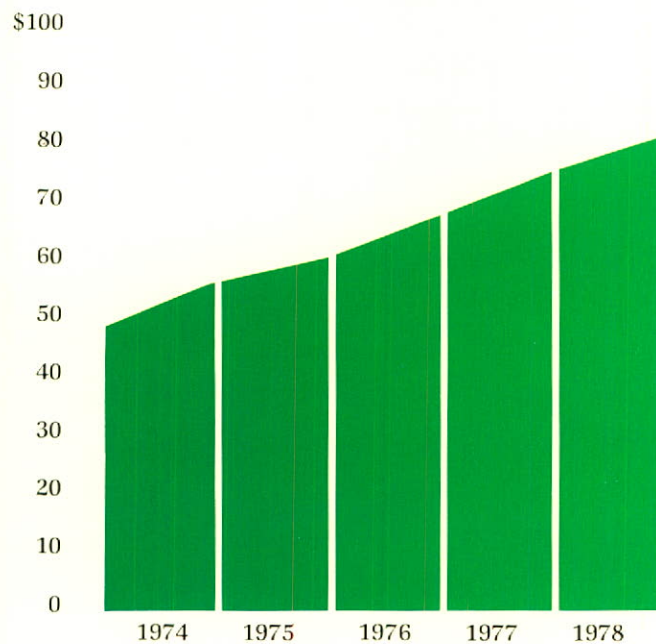
The Apparel Manufacturing Group had another record year in sales, and each of the companies within the General Retail Merchandising Group contributed to the record sales for fiscal 1978.



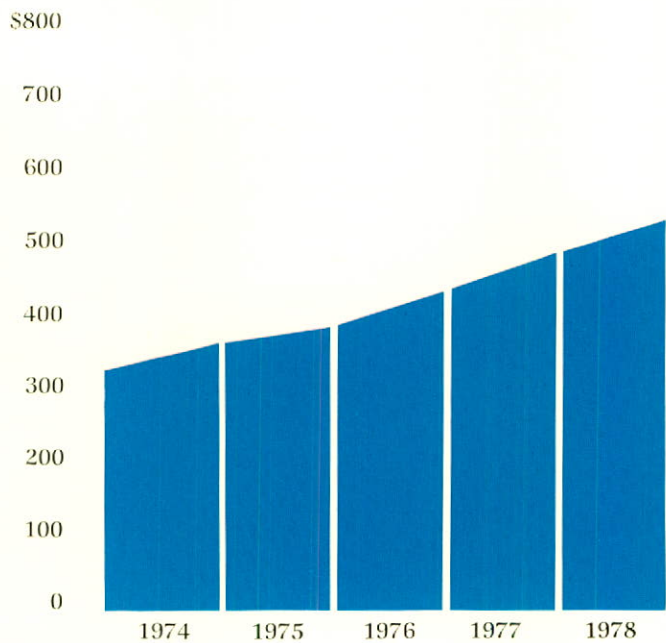
**Net Sales**  
Millions of Dollars



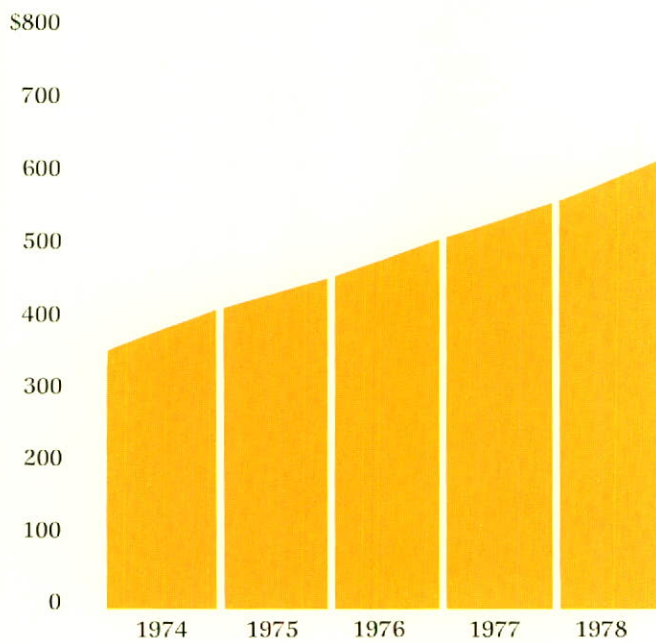
**Net Earnings**  
Millions of Dollars



**Working Capital**  
Millions of Dollars



**Stockholders' Equity**  
Millions of Dollars





# Fiscal 1978 in Review

(continued)

The Footwear Group, which includes both retailing and manufacturing, had only a modest increase in total sales, but the footwear retailing portion registered a record year, posting new volume highs.

The quarterly net sales of the company in millions of dollars were:

	<b>Fiscal 1978</b>	<b>Fiscal 1977</b>
First quarter . . . . .	\$ 378.9	\$ 376.5
Second quarter . . . . .	437.9	401.5
Third quarter . . . . .	445.3	397.7
Fourth quarter . . . . .	404.6	390.7
	<u>\$1,666.7</u>	<u>\$1,566.4</u>

## Earnings

Earnings before income taxes were a record \$161.6 million for fiscal 1978, reflecting an increase of \$12.2 million, or 8.2% higher than the restated pre-tax earnings of \$149.4 million for last year. Pre-tax earnings originally reported in fiscal 1977 were \$150.3 million.

Pre-tax earnings of each operating group of the company, before corporate expenses and interest cost, are compared in millions of dollars as follows:

	<b>Fiscal 1978</b>		<b>Fiscal 1977</b>		<b>% Change</b>
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>	
Apparel	\$ 86.7	51.2	\$ 78.0	49.0	+11.1
General Retail	38.1	22.5	32.5	20.4	+17.3
Footwear	44.6	26.3	48.8	30.6	- 8.6
	<u>\$169.4</u>	<u>100.0</u>	<u>\$159.3</u>	<u>100.0</u>	<u>+ 6.3</u>

Our Apparel Manufacturing Group and our General Retail Group which represented 73.7% of the pre-tax earnings of the company both had excellent years, establishing new earnings' records.

The Footwear Group earnings were somewhat below the strong performance of one year ago, however, our footwear retailing business, which is a part of this Group, established a new record in earnings for the fiscal 1978 year. The shoe manufacturing earnings of the footwear group were affected by lower profit margins, by a trend to more fashion-type shoes, which resulted in higher development costs, and by non-recurring expenses related to the discontinuance of the

women's shoe manufacturing business at Florsheim.

Net earnings for the year were a record \$81.8 million, an increase of 7.3% over the restated net earnings of \$76.3 million for the previous year. The net earnings for fiscal 1977 as originally reported were \$76.8 million.

Earnings per common share, fully diluted, were \$5.70 for fiscal 1978, an increase of \$0.38 per share or 7.1% over the restated \$5.32 per share earnings in fiscal 1977. Fully diluted earnings per common share originally reported for fiscal 1977 were \$5.36.

Net earnings and earnings per common share, fully diluted, for each quarter are compared in the following:

	<b>Net Earnings (In millions)</b>		<b>Net Earnings Per Share</b>	
	<b>Fiscal 1978</b>	<b>Fiscal 1977</b>	<b>Fiscal 1978</b>	<b>Fiscal 1977</b>
First quarter . . . . .	\$15.9	\$15.8	\$1.11	\$1.11
Second quarter . . . . .	19.0	17.0	1.32	1.18
Third quarter . . . . .	23.3	20.8	1.62	1.45
Fourth quarter . . . . .	23.6	22.7	1.65	1.58
	<u>\$81.8</u>	<u>\$76.3</u>	<u>\$5.70</u>	<u>\$5.32</u>

## Financial Position

The company's strong financial position continued during the 1978 fiscal year:

- ☐ Cash and marketable securities were \$113.8 million at year-end, up \$19.0 million after providing our operating needs for greater inventories, accounts receivable and capital expenditures. There was no domestic short-term borrowing during the fiscal year.
- ☐ Working capital, which is the excess of current assets over current liabilities, reached a new high of \$532.4 million at the end of fiscal 1978—a gain of \$51.2 million over the prior year. The working capital ratio was 4.2 to 1 at February 28, 1978.
- ☐ Accounts receivable were \$195.1 million at February 28, 1978—higher by 2.7% over last year and in line with the volume increase in the fourth quarter.
- ☐ Inventories were \$379.8 million, higher by 15.6% over one year ago. The higher inventories primarily reflect the increase in spring-summer advance orders in our apparel manufacturing companies, and the effect of



# Fiscal 1978 in Review

(continued)

weather-related problems in January and February, 1978 on our ability to produce and deliver our products.

- Long-term debt, including capitalized leases of \$58.3 million, less current maturities, was \$101.2 million at February 28, 1978, which is 16.3% of stockholders' equity of the company.
- Stockholders' equity was \$621.5 million at February 28, 1978 — up 10.0% from \$565.2 million at the end of fiscal 1977. The return on average stockholders' equity was 13.8% for fiscal 1978. Book value per common share increased to \$43.34 from \$39.72 one year ago.

## Capital Expenditures

The company continued its program of expansion and modernization in fiscal 1978, with capital expenditures of \$29.2 million, which included \$9.2 million of capital leases. These expenditures were for new retail stores, modernization of manufacturing plants and equipment and expansion of distributing facilities. The expenditures also include refurbishment of a number of existing retail locations.

Capital expenditures for fiscal 1979 are forecast to be \$25.0 million, with estimated depreciation of \$20.0 million.

## Dividends

Common stock shareholders received \$26.5 million in dividends, and the quarterly cash dividends paid per share were as follows:

	Fiscal 1978	Fiscal 1977
First quarter . . . . .	\$0.45	\$0.38
Second quarter . . . . .	0.45	0.41½
Third quarter . . . . .	0.45	0.41½
Fourth quarter . . . . .	0.50	0.41½

The quarterly dividend rate on common stock is currently \$0.50 per share or \$2.00 per share, annually, which became effective with the January 15, 1978 payment.

## Common Stock

There were 14,341,155 shares of common stock outstanding on February 28, 1978. There are no shares of the company's preferred stock outstanding.

The market price range per share of the company's common stock, as quoted on the New York Stock Exchange, is shown in the following:

	Fiscal 1978		Fiscal 1977	
	High	Low	High	Low
First quarter . . . . .	\$43	\$36¾	\$48¾	\$40½
Second quarter . . . . .	41⅝	37¼	43½	39⅞
Third quarter . . . . .	45⅝	38⅞	44½	40¾
Fourth quarter . . . . .	46⅞	38¾	46¼	40

The closing market price of INTERCO's common stock on February 28, 1978 was \$39.25 per share.

## Acquisitions

On March 31, 1978, after the close of the 1978 fiscal year, the company acquired all of the outstanding shares of International Hat Company for 166,635 shares of INTERCO common stock. Based upon profit performance of International Hat Company through February 28, 1981, its former stockholders could receive an additional \$2.5 million in INTERCO common stock. The number of INTERCO common shares which may be issued will be determined by the market value per share at that time.

For a full description of International Hat Company, refer to page eighteen of this report. Its operations will be included in INTERCO's reporting in fiscal 1979, from the date of acquisition.

## Operating Board

Jean S. Goodson, President of International Hat Company, was appointed to the Operating Board of INTERCO on March 31, 1978.

## Trademarks

The trademarks of INTERCO INCORPORATED and its subsidiaries, where used in the Annual Report, are italicized.

## Form 10-K—Annual Report

A copy of INTERCO INCORPORATED's current 10-K Report filed with the Securities and Exchange Commission, can be obtained by writing to: Treasurer, INTERCO INCORPORATED, Ten Broadway, St. Louis, Missouri 63102.



# Consolidated Financial Statements

INTERCO INCORPORATED



# Consolidated Balance Sheet

(Dollars in thousands)

## ASSETS

	February 28	1978	1977
Current assets:			
Cash .....	\$ 4,251	\$ 5,856	
Marketable securities .....	109,543	88,933	
Receivables, less allowances of \$9,897 (\$9,567 in 1977) .....	195,094	189,943	
Inventories .....	379,823	328,624	
Prepaid expenses and other current assets .....	8,584	9,475	
Total current assets .....	697,295	622,831	
Property, plant and equipment:			
Land .....	8,440	7,756	
Buildings and improvements .....	177,476	169,320	
Machinery and equipment .....	135,400	130,529	
	321,316	307,605	
Less accumulated depreciation .....	140,725	133,435	
Net property, plant and equipment .....	180,591	174,170	
Other assets .....	21,892	22,359	
	<u>\$899,778</u>	<u>\$819,360</u>	

See accompanying notes to consolidated financial statements.



## LIABILITIES AND STOCKHOLDERS' EQUITY

	February 28	1978	1977
Current liabilities:			
Foreign bank borrowings . . . . .	\$ 7,998	\$ 7,436	
Current maturities of long-term debt . . . . .	3,986	3,863	
Current maturities of capital lease obligations . . . . .	3,077	2,936	
Accounts payable and accrued expenses . . . . .	125,385	107,079	
Income taxes . . . . .	24,488	20,361	
Total current liabilities . . . . .	164,934	141,675	
Long-term debt, less current maturities . . . . .	42,825	46,138	
Obligations under capital leases, less current maturities . . . . .	58,325	54,056	
Other long-term liabilities . . . . .	12,182	12,313	
Stockholders' equity:			
Preferred stock, at stated and liquidating value . . . . .	—	13,613	
Common stock, at stated value . . . . .	107,559	104,148	
Capital surplus . . . . .	50,903	39,710	
Retained earnings . . . . .	463,050	407,707	
Total stockholders' equity . . . . .	621,512	565,178	
	<u>\$899,778</u>	<u>\$819,360</u>	



# Consolidated Statement of Earnings

(Dollars in thousands except per share data)

	Years Ended February 28	1978	1977
Income:			
Net sales .....		<b>\$1,666,657</b>	\$1,566,432
Other income, net .....		<b>16,625</b>	15,983
		<b><u>1,683,282</u></b>	<u>1,582,415</u>
Costs and expenses:			
Cost of sales .....		<b>1,158,387</b>	1,094,826
Selling, general and administrative expenses .....		<b>354,918</b>	330,431
Interest expense .....		<b>8,398</b>	7,766
		<b><u>1,521,703</u></b>	<u>1,433,023</u>
Earnings before income taxes .....		<b>161,579</b>	149,392
Income taxes .....		<b>79,745</b>	73,122
Net earnings .....		<b><u>\$ 81,834</u></b>	<u>\$ 76,270</u>
Per share of common stock:			
Fully diluted earnings .....		<b>\$ 5.70</b>	\$ 5.32
Primary earnings .....		<b>\$ 5.70</b>	\$ 5.43

See accompanying notes to consolidated financial statements.



# Consolidated Statement of Changes in Financial Position

(Dollars in thousands)

	Years Ended February 28	1978	1977
Working capital provided by:			
Net earnings . . . . .		\$ 81,834	\$ 76,270
Items not affecting working capital:			
Depreciation . . . . .		20,241	19,392
Other, net . . . . .		636	355
Operations . . . . .		102,711	96,017
Disposal of property, plant and equipment . . . . .		2,545	2,273
Issuance of common stock for conversion of preferred stock—contra below . . . . .		13,613	520
Issuance of common stock for restricted stock plan . . . . .		117	163
Exercise of stock options . . . . .		874	2,572
Additions to long-term debt . . . . .		673	684
Additions to capital lease obligations . . . . .		9,227	10,225
Issuance of contingent common shares . . . . .		—	652
Working capital of purchased company . . . . .		—	5,451
		<u>129,760</u>	<u>118,557</u>
Working capital used for:			
Cash dividends . . . . .		26,491	22,727
Additions to property, plant and equipment:			
Company owned property . . . . .		19,980	26,006
Leased property . . . . .		9,227	10,208
Conversion of preferred stock—contra above . . . . .		13,613	520
Reduction of long-term debt . . . . .		3,986	3,805
Reduction of capital lease obligations . . . . .		4,958	3,283
Purchase of company . . . . .		—	8,500
Other, net . . . . .		300	88
		<u>78,555</u>	<u>75,137</u>
Increase in working capital . . . . .		<u>\$ 51,205</u>	<u>\$ 43,420</u>
Working capital increased (decreased) by:			
Cash and marketable securities . . . . .		\$ 19,005	\$ 4,087
Receivables . . . . .		5,151	11,814
Inventories . . . . .		51,199	25,425
Prepaid expenses and other current assets . . . . .		( 891)	2,353
Foreign bank borrowings . . . . .		( 562)	( 7,436)
Current maturities of long-term debt . . . . .		( 123)	( 266)
Current maturities of capital lease obligations . . . . .		( 141)	( 836)
Accounts payable and accrued expenses . . . . .		(18,306)	10,053
Income taxes . . . . .		( 4,127)	( 1,774)
		<u>\$ 51,205</u>	<u>\$ 43,420</u>

See accompanying notes to consolidated financial statements.



# Consolidated Statement of Stockholders' Equity

(Dollars in thousands except per share data)

	Preferred Stock	Common Stock	Capital Surplus	Retained Earnings	Total
Balance February 29, 1976:					
As originally reported . . . . .	\$ 14,133	\$ 99,902	\$ 35,027	\$347,802	\$496,864
Adjustments for pooled company . . . . .		3,052	1,314	9,566	13,932
Adjustments for capital leases . . . . .				(2,468)	(2,468)
As restated . . . . .	14,133	102,954	36,341	354,900	508,328
Net earnings . . . . .				76,270	76,270
Cash dividends:					
Preferred stock . . . . .				(729)	(729)
Common stock — \$1.62½ per share . . . . .				(21,733)	(21,733)
By pooled company prior to combination . . . . .				(265)	(265)
Stock dividend by pooled company prior to combination — 20,185 shares . . . . .		151	505	(662)	(6)
Conversion of preferred stock:					
Series C — 5,196 shares . . . . .	(520)	119	401		
Exercise of stock options:					
Common — 100,945 shares . . . . .		757	1,815		2,572
Restricted stock plan:					
Common — 4,107 shares . . . . .		31	132		163
Issuance of 18,141 contingent common shares . . . . .		136	516		652
Adjustment to conform pooled company's fiscal year . . . . .				(74)	(74)
Balance February 28, 1977 . . . . .	13,613	104,148	39,710	407,707	565,178
Net earnings . . . . .				81,834	81,834
Cash dividends:					
Preferred stock . . . . .				(1)	(1)
Common stock — \$1.85 per share . . . . .				(26,490)	(26,490)
Conversion of preferred stock:					
Series C — 136,131 shares . . . . .	(13,613)	3,118	10,495		
Exercise of stock options:					
Common — 36,214 shares . . . . .		272	602		874
Restricted stock plan:					
Common — 2,839 shares . . . . .		21	96		117
Balance February 28, 1978 . . . . .	\$ —	\$107,559	\$ 50,903	\$463,050	\$621,512

See accompanying notes to consolidated financial statements.



# Notes to Consolidated Financial Statements

(Dollars in thousands except per share data)

## February 28, 1978 and 1977

**1. Significant Accounting Policies** — The company and its subsidiaries employ generally accepted accounting principles on a consistent basis to present fairly their consolidated financial position, results of operations, and changes in financial position. The company's fiscal year ends on the last day of February. The major accounting policies of the company are set forth below.

**Principles of Consolidation** — The consolidated financial statements include the accounts of the company and all domestic and foreign subsidiaries, the majority of which are wholly owned. All material intercompany transactions have been eliminated in consolidation.

**Marketable Securities** — Marketable securities, consisting principally of commercial paper, are stated at cost which approximates market.

**Inventories** — Inventories are stated at the lower of cost (first-in, first-out) or market, except for most footwear manufacturing inventories which are priced on the "last-in, first-out" method of inventory valuation.

**Property, Plant & Equipment** — Property, plant and equipment is stated at cost. Facilities and equipment leased under capital leases are included in property, plant and equipment with the corresponding obligations carried in obligations under capital leases. Expenditures for improvements are capitalized. Normal repairs and maintenance are expensed as incurred. When properties are retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the accounts and gains or losses on the dispositions are reflected in operations.

**Depreciation** — For financial reporting purposes, the company employs both accelerated and straight-line methods in computing depreciation. Amortization of assets recorded under capital leases is included in depreciation expense. Approximately 83% and 82% of depreciation expense was computed on the straight-line method in fiscal 1978 and fiscal 1977, respectively.

**Excess of Investment Over Equity in Subsidiaries** — Cost in excess of net assets of companies acquired is being amortized on a straight-line basis, generally over 40 years.

**Start-Up Expenses** — Start-up expenses of new facilities are charged to operations in the year incurred.

**Pension Plans** — The company's policy with respect to pension plans is to fund pension costs accrued, and to amortize prior service costs, generally over 30 years.

**Income Taxes** — Investment tax credits are reflected as a reduction of Federal income taxes in the period in which qualified property is placed in service. It is the company's intent that the undistributed earnings of subsidiaries will either be reinvested in the subsidiaries or distributed tax-free to the parent company. Accordingly, no provision has been made for income taxes on such undistributed earnings.



# Notes to Consolidated Financial Statements (continued)

**2. Business Combinations**—On January 31, 1977, the company acquired all the outstanding stock of Sky City Stores, Inc. in exchange for 427,079 shares of the company's common stock. This transaction was accounted for as a pooling of interests. Also in fiscal 1977, the company acquired Stuffed Shirt/Stuffed Jeans, Inc. in a cash transaction accounted for as a purchase.

Subsequent to February 28, 1978, the company acquired all the outstanding stock of International Hat Company in exchange for 166,635 shares of the company's common stock. Additional shares may be issued in 1981 based upon the profit performance of the acquired company. This transaction will be accounted for as a purchase.

**3. Inventories**—Inventories are summarized as follows:

	1978	1977
Retail merchandise . . . . .	\$195,086	\$ 174,840
Finished products . . . . .	81,303	71,226
Work in process . . . . .	30,710	25,280
Raw materials . . . . .	72,724	57,278
	<u>\$379,823</u>	<u>\$ 328,624</u>

All the major categories of inventory, except retail merchandise, include certain items priced on the "last-in, first-out" method. Had the "first-in, first-out" method been applied to all inventories, they would have been stated at approximately \$405,749 and \$353,709 at February 28, 1978 and 1977, respectively.

**4. Long-Term Debt**—Long-term debt consists of the following:

	1978	1977
4½% promissory installment notes, payable \$1,875 annually, 1978-1989, and balance in 1990 . . . . .	\$35,000	\$36,875
6% promissory installment notes, payable \$1,250 annually, 1978-1979, and balance in 1980 . . . . .	4,625	5,875
Foreign mortgages payable with interest rates varying from 12% to 14%, due in 1981 . . . . .	569	550
Other debt at 1% to 9½% interest rates, payable in varying amounts through 1991 . . . . .	6,617	6,701
	<u>46,811</u>	<u>50,001</u>
Less current maturities . . . . .	<u>3,986</u>	<u>3,863</u>
	<u>\$42,825</u>	<u>\$46,138</u>

Maturities of long-term debt are \$3,986, \$4,014, \$4,814, \$3,156 and \$2,491 for fiscal years 1979 through 1983, respectively.

The 4½% note agreement restricts, among other things, retained earnings of \$43,810 as to payment of cash dividends on capital stock and the purchase, redemption or retirement of capital stock.



**5. Obligations Under Capital Leases** — In fiscal 1978, the company retroactively applied the provisions of Financial Accounting Standards Board Statement No. 13 to leases with an inception date prior to January 1, 1977. The Statement requires that leases meeting certain criteria be capitalized and depreciated over their estimated useful lives, with appropriate charges to operations for the interest portion of rental payments. Net income for fiscal 1978 and fiscal 1977 decreased \$348 (\$0.02 per share) and \$489 (\$0.04 per share), respectively, as a result of this retroactive application.

The amount capitalized under capital leases is the present value of the minimum lease payments or the fair value of the leased properties at the beginning of the respective lease terms. Generally, interest rates applicable to capital leases range between 4¾% and 9% for leased facilities and between 7% and 12% for leased equipment.

Obligations under capital leases include \$38,686 in fiscal 1978 and \$41,823 in fiscal 1977 applicable to retroactive capitalization of leases with an inception date prior to January 1, 1977. Certain leases, principally from municipalities under industrial financing arrangements and leases of equipment, both of which have provisions for purchase options, were capitalized in prior years and included in long-term debt. Long-term debt reclassified to obligations under capital leases for fiscal 1977 amounted to \$12,233.

Maturities of obligations under capital leases are \$3,077, \$2,973, \$2,947, \$3,041 and \$3,192 for fiscal years 1979 through 1983, respectively.

**6. Preferred Stock** — The company's preferred stock is issuable in series. Authorized preferred stock consists of 577,060 shares of first preferred and 1,000,000 shares of second preferred, both without par value.

At February 28, 1977, the outstanding preferred stock consisted of 136,131 shares of Series C, \$5.25 Cumulative Convertible Second Preferred Stock with stated and involuntary liquidating value of \$100 per share.

In March 1977, all the Series C preferred stock was converted into 415,643 shares of common stock at the conversion rate of 3.0534 shares of common stock for one share of preferred stock, and 19.3954 fractional shares were redeemed for cash.



# Notes to Consolidated Financial Statements (continued)

**7. Common Stock**—The company's common stock consists of 50,000,000 shares authorized with stated value of \$7.50 per share, of which 14,341,155 and 13,886,459 shares were issued at February 28, 1978 and 1977, respectively.

Shares of common stock were reserved for the following purposes at February 28, 1978:

	<b>Number of Shares</b>
Common stock options:	
Granted .....	144,439
Available for grant .....	318,200
Restricted stock plan	
of pooled company .....	7,569
	<u>470,208</u>

Under the company's stock option plans, certain key employees may be granted qualified or non-qualified options to purchase

shares of common stock. Qualified options granted under the plans may not be less than 100% of the fair market value of the common stock on the date an option is granted, and non-qualified options at not less than 85%. Qualified options are exercisable at varying dates one year after granting and expire five years after granting. Non-qualified options become exercisable one year after granting and expire ten years after granting. All options which have been granted, qualified and non-qualified, were at 100% of fair market value on the date of grant.

Changes in options granted are summarized as follows:

	<b>1978</b>		<b>1977</b>	
	<b>Shares</b>	<b>Average Price</b>	<b>Shares</b>	<b>Average Price</b>
Beginning of year .....	136,978	\$23.47	228,375	\$20.72
Options granted .....	48,964	38.55	15,450	43.26
Options exercised .....	( 36,214)	20.69	(100,945)	20.07
Options cancelled .....	( 5,289)	33.79	( 5,902)	27.11
End of year .....	<u>144,439</u>	<u>28.90</u>	<u>136,978</u>	<u>23.47</u>
Exercisable at end of year .....	<u>56,060</u>		<u>72,467</u>	



**8. Income Taxes** — Income tax expense is composed of the following:

	1978	1977
Current:		
Federal .....	\$67,947	\$64,339
State and city .....	8,257	7,301
Foreign (principally Canadian) .....	1,289	2,083
	<u>77,493</u>	<u>73,723</u>
Deferred .....	2,252	( 601)
	<u>\$79,745</u>	<u>\$73,122</u>
Investment tax credits .....	\$ 1,244	\$ 1,646

Certain items are recognized for income tax purposes in years other than those in which they are reported in the consolidated financial statements. The tax effect of such differences resulted in net deferred income taxes summarized as follows:

	1978	1977
Depreciation .....	\$ 791	\$ 552
Installment sales .....	( 32)	198
Retroactive capitalization of capital leases .....	( 322)	( 453)
Valuation reserves and accruals .....	1,804	( 636)
Deferred compensation .....	( 218)	157
Adjustments resulting from audit of prior years' tax returns .....	179	( 420)
Other .....	50	1
	<u>\$2,252</u>	<u>\$( 601)</u>

Future Federal income tax benefits at February 28, 1978 and 1977 are included in the accompanying consolidated balance sheet as follows:

	1978	1977
Prepaid expenses and other current assets .....	\$2,623	\$4,418
Other assets .....	3,598	4,055
	<u>\$6,221</u>	<u>\$8,473</u>

The Federal income tax returns of the company and its major subsidiaries for fiscal 1976 and 1975 are currently in the process of examination. Management does not expect the results of these examinations to have a material effect on consolidated financial position or results of operations.

**9. Pension Plans** — The company and its subsidiaries have pension plans covering substantially all employees. Total pension expense was \$13,500 and \$11,900 in fiscal 1978 and fiscal 1977, respectively. As of the most recent valuation dates, the actuarially computed value of vested benefits under defined benefit pension plans exceeded assets of the plans by approximately \$41,100.

**10. Lease Commitments** — Substantially all of the company's retail outlets and certain other real properties and equipment are operated under lease agreements expiring at various dates through the year 2003. Leases covering retail outlets and equipment generally require, in addition to stated minimums, contingent rentals based on retail sales and equipment usage. Generally, the leases provide for renewal for various periods at stipulated rates.

Assets recorded under capital leases includes leases capitalized in prior years, retroactive capitalization of capital leases and current year additions, as follows:

	1978	1977
Land .....	\$ 699	\$ 699
Buildings .....	62,206	56,447
Machinery and equipment .....	8,062	8,759
	<u>70,967</u>	<u>65,905</u>
Accumulated depreciation .....	18,339	16,863
	<u>\$52,628</u>	<u>\$49,042</u>

Future minimum lease payments under capital leases at February 28, 1978, aggregate \$122,381, of which \$61,402 is included in obligations under capital leases and current maturities, \$50,876 represents interest and the balance represents other costs of the leases including taxes, insurance and maintenance. Annual payments under capital leases are \$8,892, \$8,487, \$8,178, \$7,995 and \$7,828 for the fiscal years 1979 through 1983, respectively.



# Notes to Consolidated Financial Statements (continued)

Lease costs under operating leases and contingent costs of capital leases are considered rental expense. Total rental expense was as follows:

	1978	1977
Basic rentals under operating leases . . . . .	\$26,672	\$27,007
Contingent rentals . . . . .	16,994	14,176
	43,666	41,183
Less sublease rentals . . . . .	1,213	1,288
	<u>\$42,453</u>	<u>\$39,895</u>

Included in rental expense above is the cost of services provided by lessors of leased retail departments, estimated to aggregate \$7,200 and \$6,900 in fiscal 1978 and fiscal 1977, respectively.

Future minimum lease payments under operating leases at February 28, 1978, aggregate \$159,962. Annual payments under operating leases are \$22,908, \$20,891, \$18,452, \$15,825 and \$14,054 for the fiscal years 1979 through 1983, respectively.

The minimum rental commitments have been reduced by rentals from subleases. These subleases, expiring at various dates to 1994, provide for aggregate minimum rentals of approximately \$2,600.

The company has also guaranteed leases of certain retail outlets of customers which at February 28, 1978, aggregated approximately \$2,100 based on minimum rentals.

**11. Litigation**—The company is a defendant and may become a defendant in a number of pending or threatened legal proceedings in the ordinary course of business. In the opinion of management, the ultimate liability, if any, of the company from all such proceedings will not have a material adverse effect upon the consolidated financial position or results of operations.

The Federal Trade Commission is currently investigating the marketing and distribution methods of the women's apparel industry, and a number of the company's women's apparel manufacturing companies have furnished the Commission with information in this regard. A similar investigation has been undertaken with respect to certain footwear manufacturing operations of the company and one men's apparel manufacturing subsidiary. Should the Commission issue a complaint as a result of said investigations, any final resolution of such matters will not have a material adverse effect upon the company.

## 12. Earnings Per Share of Common Stock—

Fully diluted earnings per share are based on the weighted average number of shares of common stock and common stock equivalents outstanding during the years, plus those common shares which would have been issued if conversion of all preferred stock had taken place at the beginning of each year. Common stock options, the exercise of which would result in dilution of earnings per share, are considered common stock equivalents.

Primary earnings per share are based on those shares included in the fully diluted earnings per share calculations, except that conversion of preferred stock has not been assumed. Net earnings for this computation are reduced by preferred stock dividend requirements.



**13. Business Segment Information**—The company's three business segments are Apparel Manufacturing, General Retail Merchandising, and Footwear Manufacturing and Retailing. Specific information relating to the operating companies and their products which comprise each segment is included on pages four through seventeen of the Annual Report.

Summarized financial information by business segments is as follows:

	1978	1977
Sales to unaffiliated customers:		
Apparel . . . . .	\$ 640,487	\$ 576,019
Retail . . . . .	521,178	498,557
Footwear . . . . .	504,992	491,856
Total . . . . .	<u>\$1,666,657</u>	<u>\$1,566,432</u>
Operating profit:		
Apparel . . . . .	\$ 86,745	\$ 78,050
Retail . . . . .	38,096	32,473
Footwear . . . . .	44,552	48,768
	169,393	159,291
Corporate expenses and interest cost . . . . .	( 7,814)	( 9,899)
Earnings before income taxes . . . . .	<u>\$ 161,579</u>	<u>\$ 149,392</u>
Identifiable assets at year end:		
Apparel . . . . .	\$ 295,518	\$ 264,578
Retail . . . . .	238,569	213,064
Footwear . . . . .	258,572	253,096
	792,659	730,738
Corporate assets . . . . .	107,119	88,622
Total . . . . .	<u>\$ 899,778</u>	<u>\$ 819,360</u>
Depreciation expense:		
Apparel . . . . .	\$ 6,287	\$ 5,801
Retail . . . . .	7,267	6,798
Footwear . . . . .	6,209	6,379
Capital expenditures including capital leases:		
Apparel . . . . .	\$ 8,704	\$ 12,326
Retail . . . . .	14,140	14,179
Footwear . . . . .	5,959	8,304

Sales between business segments, which account for less than 1% of the sales of any one business segment, are considered immaterial and are netted against the sales of the respective segment. Operating profit of the business segment is its sales less all operating expenses. Minority interests in certain subsidiaries are immaterial and have been included in corporate expenses and interest cost.

Identifiable assets of a business segment are those assets that are used by that segment in its operations. Corporate assets consist primarily of cash and marketable securities.

Substantially all of the company's sales are made to unaffiliated customers and no one customer accounted for 10% of the consolidated sales. Foreign operations are not material in relation to the consolidated financial position or results of operations.



# Notes to Consolidated Financial Statements (continued)

## 14. Quarterly Financial Information

(Unaudited) — The following unaudited quarterly information includes all adjustments and is restated to include retroactive capitalization of leases:

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
<b>Fiscal 1978</b>				
Net sales .....	\$378,882	\$437,867	\$445,341	\$404,567
Gross profit .....	114,025	124,959	134,817	134,469
Earnings before income taxes .....	31,943	38,354	45,718	45,564
Net earnings .....	<u>\$ 15,948</u>	<u>\$ 18,984</u>	<u>\$ 23,284</u>	<u>\$ 23,618</u>
Net earnings per share:				
Fully diluted .....	\$1.11	\$1.32	\$1.62	\$1.65
Primary .....	<u>\$1.11</u>	<u>\$1.32</u>	<u>\$1.62</u>	<u>\$1.65</u>
As previously reported:				
Net sales .....	\$378,882	\$437,867	\$445,341	
Net earnings .....	<u>\$ 16,071</u>	<u>\$ 19,104</u>	<u>\$ 23,400</u>	
<b>Fiscal 1977</b>				
Net sales .....	\$376,531	\$401,452	\$397,712	\$390,737
Gross profit .....	109,210	114,487	122,735	125,174
Earnings before income taxes .....	31,836	34,128	40,950	42,478
Net earnings .....	<u>\$ 15,828</u>	<u>\$ 16,946</u>	<u>\$ 20,824</u>	<u>\$ 22,672</u>
Net earnings per share:				
Fully diluted .....	\$1.11	\$1.18	\$1.45	\$1.58
Primary .....	<u>\$1.13</u>	<u>\$1.20</u>	<u>\$1.49</u>	<u>\$1.61</u>
As previously reported:				
Net sales .....	\$376,531	\$401,452	\$397,712	\$390,737
Net earnings .....	<u>\$ 15,944</u>	<u>\$ 17,071</u>	<u>\$ 20,952</u>	<u>\$ 22,792</u>



**15. Replacement Cost Data** (Unaudited) — The Securities and Exchange Commission requires many large companies to report certain information relating to replacement cost of inventories and fixed assets, and the impact of these costs upon depreciation and cost of sales.

In the normal course of business, the company has been able and will continue to replace its productive capacity in an orderly manner. Historically, the company has been able to compensate for cost increases through increases in productivity and selling prices in order to maintain an approximately constant gross profit percentage of sales.

Due to inflation and the cost of technological improvements, the replacement of plant and equipment with assets having equivalent productive capacity has usually required a substantially greater capital investment than was required to purchase the assets which were being replaced. The additional capital investment principally reflects the cumulative impact of inflation on the long-lived nature (approximately 10 years for machinery and 25 years for buildings) of these assets.

The company's annual report on Form 10-K (a copy of which is available upon request) will contain more specific information with respect to replacement cost of inventories and productive capacity (buildings, machinery, and equipment), and the approximate effect which replacement cost would have had on the computation of cost of sales and depreciation expense for fiscal 1978 and fiscal 1977.

**PEAT, MARWICK, MITCHELL & CO.**

Certified Public Accountants  
720 Olive Street  
St. Louis, Missouri  
THE BOARD OF DIRECTORS  
AND STOCKHOLDERS  
INTERCO INCORPORATED:

We have examined the consolidated balance sheets of INTERCO INCORPORATED and subsidiaries as of February 28, 1978 and 1977 and the related consolidated statements of earnings, stockholders' equity, and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of INTERCO INCORPORATED and subsidiaries at February 28, 1978 and 1977 and the results of their operations, and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

*Peat, marwick, mitchell & Co.*

April 12, 1978



# Five Year Consolidated Financial Review

(Dollars in thousands except per share data)

	FISCAL YEARS ENDED				
	1978	1977	1976	1975	1974
<b>FOR THE YEAR</b>					
Summary of operations:					
Net sales . . . . .	<b>\$1,666,657</b>	\$1,566,432	\$1,424,252	\$1,373,223	\$1,304,874
Cost of sales . . . . .	<b>1,158,387</b>	1,094,826	992,754	963,801	921,522
Interest expense . . . . .	<b>8,398</b>	7,766	6,901	8,743	8,252
Earnings before income taxes	<b>161,579</b>	149,392	135,785	121,087	110,599
As a percent of sales . . . . .	<b>9.7%</b>	9.5%	9.5%	8.8%	8.5%
Income taxes . . . . .	<b>79,745</b>	73,122	67,212	59,853	53,799
Net earnings . . . . .	<b>81,834</b>	76,270	68,573	61,234	56,800
As a percent of sales . . . . .	<b>4.9%</b>	4.9%	4.8%	4.5%	4.4%
Earnings applicable to common stock . . . . .	<b>81,834</b>	75,541	67,799	60,386	55,934
Per share of common stock:					
Fully diluted earnings (1) . .	<b>\$5.70</b>	\$5.32	\$4.81	\$4.31	\$4.02
Dividends . . . . .	<b>\$1.85</b>	\$1.62½	\$1.47½	\$1.43½	\$1.32
Average common and common equivalent shares outstanding (in thousands) (1) . . . . .					
	<b>14,365</b>	14,324	14,268	14,207	14,140
Cash dividends paid:					
On common stock . . . . .	<b>\$26,490</b>	\$21,998	\$18,150	\$17,270	\$14,418
On preferred stock . . . . .	<b>\$ 1</b>	\$ 729	\$ 791	\$ 850	\$ 868
<b>AT YEAR END</b>					
Working capital . . . . .	<b>\$532,361</b>	\$481,156	\$437,736	\$395,615	\$361,636
Property, plant and equipment, net . . . . .	<b>180,591</b>	174,170	156,047	149,365	142,034
Capital expenditures:					
Company owned property . .	<b>19,980</b>	26,006	21,698	21,158	22,848
Capitalized leased property . .	<b>9,227</b>	10,208	3,486	5,513	12,155
Total assets . . . . .	<b>899,778</b>	819,360	755,387	673,097	656,747
Long-term debt . . . . .	<b>42,825</b>	46,138	47,443	50,576	53,773
Obligations under capital leases	<b>58,325</b>	54,056	46,069	44,825	43,946
Stockholders' equity . . . . .	<b>621,512</b>	565,178	508,328	456,995	413,901
Book value per common share .	<b>\$43.34</b>	\$39.72	\$36.00	\$32.73	\$29.67

(1) Refer to Earnings Per Share of Common Stock in Notes to Consolidated Financial Statements.

(2) The above figures have been restated to include pooled companies for years prior to their acquisition and for the retroactive restatement of capital leases.

(3) Fiscal years end the last day in February.



# Management's Discussion and Analysis of Operations

**Net Sales**—Sales for fiscal 1978 again established a new record with an increase of 6.4% over fiscal 1977 compared to a 10.0% increase for fiscal 1977 over fiscal 1976. The increase during those two years was principally attributable to increased market acceptance of our products and to higher selling prices relating to increased raw material, labor and operating costs. While the sales for the fourth quarter of fiscal 1978 and fiscal 1977 were records, they were adversely affected by the severe winter weather conditions and reflected increases of only 3.5% and 3.3%, respectively, when compared to the preceding year.

The Apparel Manufacturing Group attained an 11.2% sales increase for fiscal 1978, as compared to a 19.0% increase in the prior year. The General Retail Merchandising Group had a sales increase of 4.5% after a 5.1% increase last year. The Footwear Manufacturing and Retailing Group showed a 2.7% sales increase following a 5.6% increase in fiscal 1977.

**Cost of Sales and Operating Expenses**—Cost of sales and operating expenses combined were 90.8% of sales in fiscal 1978 and 91.0% in fiscal 1977.

Cost of sales, as a percent of sales, was 69.5% in fiscal 1978 and 69.9% in fiscal 1977. On a comparative basis, the increase was 5.8% for fiscal 1978 and 10.3% for fiscal 1977. The improvement in fiscal 1978 was principally attributable to higher markups attained by the General Retail Merchandising Group which had experienced above-normal markdowns in fiscal 1977. The Apparel Manufacturing Group had a slight improvement in gross profit margins on increased volume and higher selling prices, while the Footwear Manufacturing and Retailing Group recorded higher costs which could not be fully passed on to customers.

As a percent of sales, operating expenses were 21.3% and 21.1% for fiscal 1978 and fiscal 1977, respectively. These expenses

increased 7.4% in fiscal 1978 as compared to an 8.8% increase in the prior year. The increases can be mainly attributable to higher operating costs in most categories and to the severe winter weather which forced the closing of a number of distribution centers and the curtailment of store hours in some shopping centers and other retail locations in both years.

**Interest Expense**—For fiscal 1978 and fiscal 1977, substantially all the interest expense is attributable to the long-term debt and obligations under capital leases. Interest expense increased by \$632,000, or 8.1%, in fiscal 1978 as compared to an increase of \$865,000, or 12.5%, in fiscal 1977, and these increases represent the additional costs in connection with capital leases. The only short-term debt during either year was for bank borrowings of the foreign subsidiaries. Fiscal 1976 interest expense decreased from the prior year by \$1,842,000 due to the reduction in short-term borrowing and corresponding interest rates.

**Earnings Before Income Taxes**—Earnings before income taxes increased by 8.2% in fiscal 1978 as compared to a 10.0% increase in fiscal 1977. The increase in fiscal 1978 can be attributed to the improvement in gross profit margins of the Apparel Manufacturing and General Retail Merchandising Groups. The fiscal 1977 increase relates to the percentage increase in sales, with cost of sales and operating expenses remaining constant, as a percent of sales, with those of the preceding year.

**Income Taxes**—Income taxes for fiscal 1978 increased by 9.1% with an effective tax rate of 49.4% compared to an increase last year of 8.8% and an effective tax rate of 48.9%. After adjustment for investment tax credits received in the respective year, the increases correspond directly to the improvement in earnings before income taxes.



# Directors, Officers and the Operating Board

## Board of Directors

- \*RONALD L. AYLWARD  
Vice President and  
General Counsel of the  
Company
- \*MAURICE R. CHAMBERS  
Chairman of the Executive  
Committee of the Company
- \*STANLEY M. COHEN  
President, Central  
Hardware Company
- \*WILLIAM L. EDWARDS, JR.  
Chairman of the Board and  
Chief Executive Officer of  
the Company
- †RICHARD P. HAMILTON  
President, The Florsheim  
Shoe Company
- \*PHILIP N. HIRSCH  
Chairman of the Board,  
P. N. Hirsch & Company
- \*J. LEE JOHNSON  
Retired
- EDWIN S. JONES  
Chairman of the Executive  
Committee, First  
Union Bancorporation  
and First National Bank  
in St. Louis
- DONALD E. LASATER  
Chairman of the Board,  
Mercantile Bancorporation  
Inc. and Mercantile Trust  
Company National Association
- \*NORFLEET H. RAND  
Retired
- \*JOHN K. RIEDY  
President and Chief  
Operating Officer of  
the Company
- HERBERT SHAINBERG  
Retired

## Audit Committee

J. Lee Johnson, Chairman  
Maurice R. Chambers  
Edwin S. Jones  
Donald E. Lasater  
Norfleet H. Rand

## Executive Compensation and Stock Option Committee

Maurice R. Chambers, Chairman  
J. Lee Johnson  
Edwin S. Jones  
Donald E. Lasater  
Norfleet H. Rand

## Corporate Officers

- WILLIAM L. EDWARDS, JR.  
Chairman of the Board and  
Chief Executive Officer
- JOHN K. RIEDY  
President and Chief  
Operating Officer
- PHILIP N. HIRSCH  
Vice President
- STANLEY M. COHEN  
Vice President
- †RICHARD P. HAMILTON  
Vice President
- RONALD L. AYLWARD  
Vice President and  
General Counsel
- DUANE A. PATTERSON  
Secretary
- EDWARD P. GRACE  
Treasurer
- STANLEY F. HUCK  
Controller
- KEITH E. MATTERN  
Assistant Secretary
- JAMES K. PENDLETON  
Assistant Secretary
- WILLIAM R. WITTHROW  
Assistant Treasurer
- RUSSELL L. BAUMANN  
Assistant Controller

\*Members of the Executive  
Committee of the Board of  
Directors

†Resigned April 21, 1978

## Operating Board

- WILLIAM L. EDWARDS, JR.  
Chairman of the Board and  
Chief Executive Officer of  
the Company
- JOHN K. RIEDY  
President and Chief Operating  
Officer of the Company
- RONALD L. AYLWARD  
Vice President and  
General Counsel of  
the Company
- LIONEL BAXTER  
President,  
Big Yank Corporation
- STANLEY M. COHEN  
President,  
Central Hardware Company
- WILLIAM B. COWDEN  
President, Cowden  
Manufacturing Company
- BARRY S. FINE  
President,  
Fine's Men's Shops, Inc. and  
Standard Sportswear, Inc.
- JEAN S. GOODSON  
President,  
International Hat Company
- †RICHARD P. HAMILTON  
President,  
The Florsheim Shoe Company
- GERALD B. HIRSCH  
President,  
P. N. Hirsch & Company
- DONALD G. MacLEOD  
President,  
Intervo Savage Limited
- STANLEY MATZKIN  
President, Devon Apparel, Inc.
- JONATHAN P. MYERS  
President,  
Londontown Corporation
- MYRON C. PETERSON  
Chairman of the Board and  
President, Sky City Stores, Inc.
- J. CARL POWERS  
President,  
International Shoe Company
- HARVEY ROTHENBERG  
Chairman of the Board,  
Stuffed Shirt/Stuffed Jeans, Inc.
- CHARLES J. ROTHSCHILD, JR.  
President, Campus Sweater &  
Sportswear Company
- HARVEY SALIGMAN  
President, Queen Casuals, Inc.
- ARTHUR SIBLEY  
President, College-Town, Inc.
- JOHN WEIL  
President, Eagle Family  
Discount Stores, Inc.



# Principal Companies of INTERCO

## Apparel Manufacturing Group

BIG YANK CORPORATION  
New York, New York

THE BILTWELL COMPANY, INC.  
St. Louis, Missouri

CAMPUS SWEATER &  
SPORTSWEAR COMPANY  
New York, New York

COLLEGE-TOWN, INC.  
Braintree, Massachusetts

COWDEN MANUFACTURING  
COMPANY  
Lexington, Kentucky

DEVON APPAREL, INC.  
Philadelphia, Pennsylvania

INTERNATIONAL HAT  
COMPANY  
St. Louis, Missouri

LONDONTOWN CORPORATION  
Eldersburg, Maryland

QUEEN CASUALS, INC.  
Philadelphia, Pennsylvania

SIDNEY GOULD CO., LTD.  
Garden City Park, New York

STUFFED SHIRT/  
STUFFED JEANS, INC.  
New York, New York

## General Retail Merchandising Group

CENTRAL HARDWARE  
COMPANY  
St. Louis, Missouri

EAGLE FAMILY DISCOUNT  
STORES, INC.  
Miami, Florida

FINE'S MEN'S SHOPS, INC.  
Norfolk, Virginia

GOLDE'S DEPARTMENT  
STORES, INC.  
St. Louis, Missouri

P. N. HIRSCH & COMPANY  
St. Louis, Missouri

SKY CITY STORES, INC.  
Asheville, North Carolina

STANDARD SPORTSWEAR, INC.  
Pittsburgh, Pennsylvania

UNITED SHIRT  
DISTRIBUTORS, INC.  
Detroit, Michigan

## Footwear Manufacturing and Retailing Group

THE FLORSHEIM SHOE  
COMPANY  
Chicago, Illinois

INTERNATIONAL SHOE  
COMPANY  
St. Louis, Missouri

INTERCO SAVAGE LIMITED  
Cambridge, Ontario, Canada

SENACK SHOES, INC.  
St. Louis, Missouri

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## Transfer Agents

Manufacturers Hanover  
Trust Company  
New York, New York

Mercantile Trust Company  
National Association  
St. Louis, Missouri

## Registrars

Morgan Guaranty  
Trust Company  
New York, New York

St. Louis Union  
Trust Company  
St. Louis, Missouri

## Dividend Disbursing Agent

Mercantile Trust Company  
National Association  
St. Louis, Missouri

## Independent Accountants

Peat, Marwick, Mitchell & Co.  
St. Louis, Missouri

## Exchange Listings

Symbol	Listed
ISS	New York Stock Exchange
ISS	Midwest Stock Exchange

## Corporate Offices

Ten Broadway  
St. Louis, Missouri 63102  
(314) 231-1100

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Post Office Box 8777  
St. Louis, Missouri 63102



INTERCO INCORPORATED • St. Louis, Missouri